Single Electricity Market

(SEM)

Capacity Market Code

Terms of Reference for the Year 8 Market Audit - Decision Paper

SEM-26-72

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1. BACKGROUND

Paragraph B.11.2.1 of the Capacity Market Code (CMC) requires the Market Auditor to conduct an audit of the operation and implementation of the arrangements, procedures, and processes under the CMC at least once a year.

Paragraph B.11.2.3 of the Code requires the Regulatory Authorities (RAs) to consult with Parties on the Terms of Reference (ToR) for the audit. The last Audit Report was published on 11 September 2026. Paragraph B.11.2.3 requires the RAs to consult with Parties on the terms of reference for the next audit following publication of the Audit Report. Paragraph B.11.2.4 requires the RAs to annually specify the precise ToR for the audit following a consultation process.

The purpose of this paper is to set out the SEM Committee's decision on the scope of the Year 8 audit together with the reporting arrangements.

The RAs revisited the original ToR set out in SEM-17-023[1] alongside the Year 7 ToR Decision Paper and considered whether the scope for the Year 8 audit should be changed.

2. PROPOSED YEAR 8 AUDIT SCOPE

The SEM Committee proposed that the Year 8 audit cover the twelve-month period of 1 October 2025 to 30 September 2026. The audit would incorporate the following Capacity Auctions:

- T-4 2029/2030 Capacity Auction - which took place on 26 March 2026
- T-1 2026/2027 Capacity Auction - which took place on 23 July 2026

The 17-month audit period adopted last year realigned the audit cycle with the Capacity Year, allowing Year 8 and subsequent audits to cover a standard 12-month period.

The SEM Committee also recommended that the Auditor's Opinion continue to be provided under the International Standard on Assurance Engagements (ISAE 3000) and that the Year 8 audit use ToR similar to those established for Year 7.

[1] SEM-17-023

The proposed ToR for the Year 8 included:

- Accession and Registration.
- Default, Suspension and Termination.
- Qualification.
- Operation of the auction and award of capacity.
- Secondary trading.
- Implementation agreements.
- SO, and other Charges.
- Invoicing and Payment.
- Credit Cover management.
- Disputes.
- Modifications.
- Design Authority / Code development and Systems Upgrade.
- The materiality threshold will be based on 0.5% of the average Capacity Requirement at market level.
- A threshold of 10% of materiality will be used for the reporting of significant issues.

3. SUMMARY OF RESPONSES

The SOs propose increasing the CMC audit materiality threshold from 0.5% to 1% of the relevant MW benchmark, increasing the proposed Year 8 threshold from 34.088 MW to 67.493 MW. The SOs argue that the current 0.5% MW threshold is not directly comparable with the 0.5% financial materiality threshold used for the Trading and Settlement Code audit. When the 34.088 MW threshold is translated into financial terms and compared with Total Capacity Payments, the SOs calculate that it represents an effective financial materiality threshold of 0.28%. The SOs therefore consider that a 1% MW threshold would provide closer alignment with a 0.5% financial materiality threshold, while noting that all findings identified through the audit would continue to be reported.

4. SEM COMMITTEE RESPONSE

The SEM Committee welcomes the response received in conjunction with consultation SEM-26-35.

The SEM Committee acknowledges the SOs' rationale for proposing an increase in the materiality threshold from 0.5% to 1%. However, the current methodology was introduced only for the Year 7 audit, following a proposal from the SOs to replace the previous fixed 20 MW threshold with a threshold based on 0.5% of the average Capacity Requirement. Given that the revised methodology has only been applied for one audit cycle, the SEM Committee considers that there is limited practical experience of its operation and that a further substantive change would be premature at this stage.

In addition, increasing the threshold to 1% would result in a significant increase in the materiality threshold, from the original fixed threshold of 20 MW to 67.493 MW for the Year 8 audit period.

The Year 7 audit also highlighted the limitations of applying a purely volumetric measure of materiality across all aspects of the CMC. A number of the findings related to financial, procedural, governance or control requirements and did not necessarily have a readily identifiable MW impact. As the CMC requires the Capacity Market Auditor to consider the operation and implementation of the arrangements, procedures and processes under the Code, the SEM Committee considers it important that the audit framework maintains an appropriate level of scrutiny across the full range of CMC obligations.

While findings below the materiality threshold would continue to be reported, increasing the threshold would nevertheless increase the quantitative level at which identified non-compliance could affect the overall audit conclusion. The SEM Committee therefore considers it appropriate to retain the 0.5% threshold for Year 8, allowing a further audit cycle to assess how the revised methodology operates before considering whether further changes are warranted.

5. SEM COMMITTEE DECISION

The SEM Committee has decided to implement the following approach and ToR for the Year 8 Capacity Market Audit:

Timescale

The SEM Committee has decided that the Year 8 audit will cover the twelve-month period between 1 October 2025 to 30 September 2026. The audit will incorporate the following Capacity Auctions:

- T-4 2029/2030 Capacity Auction - which took place on 26 March 2026
- T-1 2026/2027 Capacity Auction - which took place on 23 July 2026

Reporting

The Auditor's Opinions for the previous seven annual audits were provided under the International Standard on Assurance Engagements (ISAE 3000). Taking account of the requirement under ISAE 3000 for the Auditor to provide an assurance opinion, the SEM Committee has decided that the Year 8 audit will continue to be conducted under ISAE 3000.

Terms of Reference

It is the SEM Committee's view that the Year 8 Capacity Market Audit report will include:

- Accession and Registration;
- Default, Suspension and Termination;
- Qualification;
- Operation of the auction and award of capacity;
- Secondary Trading;
- Implementation agreements;
- SO, and other Charges;
- Invoicing and Payment;
- Credit Cover management;
- Disputes;
- Modifications; and
- Design Authority / Code development and Systems Upgrade;
- Materiality threshold will be based on 0.5% of market level. Market level materiality for the Year 8 audit period is calculated as follows:
  ((7112+6523) / 2) * 0.5% = **34.088 MW**
  - A threshold of 10% of materiality will be used for the reporting of significant issues.

6. NEXT STEPS

Following publication of this paper, the Capacity Market Auditor will complete the Year 8 audit.